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No. 71-1316

In the Supreme Court of the United States

OCTOBER TERM, 1971

EMORY K. CRENSHAW, AS EXECUTOR OF THE ESTATE OF FRANCES WOOD WILSON, DECEASED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The opinion of the district court (Pet. App. 19-26) is unofficially reported at 70-2 U.S.T.C., par. 9530. The opinion of the court of appeals (Pet. App. 27-36) is not yet officially reported.

JURISDICTION

The court of appeals on October 22, 1971, reversed the judgment of the district court and remanded the cause for entry of judgment in favor of the United States (Pet. App. 27, 36). A petition for rehearing and petition for rehearing *en banc* were denied on January 14, 1972 (Pet. App. 37). The petition for a

writ of certiorari was filed on April 13, 1972. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the court of appeals correctly held that a planned series of transactions whereby petitioner [1] withdrew from a partnership constituted a taxable sale of her partnership interest to the remaining partners under Section 741 of the Internal Revenue Code of 1954 rather than a nontaxable liquidation of her interest by the partnership under Section 736(b).

STATUTES AND REGULATIONS INVOLVED

The pertinent provisions of the Internal Revenue Code of 1954 and the Regulations thereunder are set forth in the appendix to the petition (pp. 39–41).

STATEMENT

Petitioner, in November 1962, was the owner of a 50/225 interest in the Pine Forest Associates partnership. The remaining partnership interests were owned by Leon Blair and his wife Julien. Mr. Blair contacted the petitioner's attorney with an offer to purchase her interest for cash, and in response to this offer, the attorney informed Mr. Blair that the petitioner was willing to dispose of her interest, but that, in view of her general financial position, an exchange of the interest for other income-producing property would be more in accord with her needs than a sale.

[1] Decedent, Frances Wood Wilson, is referred to herein as "petitioner."

(Pet. App. 28.) Although Mr. Blair did not then own property suitable for this purpose, subsequent discussions revealed that a suitable piece of property could be obtained from the estate of the petitioner's husband. A plan was then formulated, the end result of which would provide the petitioner with income-producing property, while retaining in the partnership the undivided 50/225 interest in certain property (The Pine Forest Apartments) purportedly distributed to petitioner in liquidation of her partnership interest (Pet. App. 29). Thereafter, in accordance with that plan, the following events occurred (Pet. App. 29):

(1) Petitioner withdrew from the partnership in exchange for an undivided 50/225 interest in a parcel of real estate (Pine Forest Apartments) owned by the partnership;

(2) Acting individually and as executrix of her husband's estate, petitioner transferred the undivided 50/225 interest in the Pine Forest Apartments for other real estate (Oglethorpe Shopping Center) belonging to the estate;

(3) Acting as executrix of her husband's estate, petitioner transferred the undivided 50/225 interest in the Pine Forest property to a new corporation (Blair Investment Company, all of whose stock was owned by Mr. and Mrs. Blair) for $200,000 cash; and

(4) The Blair Investment Company then retransferred the undivided 50/225 interest in the Pine Forest property back to the partnership in exchange

for the partnership interest formerly owned by the petitioner.[2]

On her income tax return for the taxable year 1962, petitioner treated the above-described transactions as a nontaxable distribution of partnership property in liquidation of her partnership interest under Sections 731 and 736(b) of the 1954 Code, followed by a tax-free exchange of the property distributed for other income-producing property. The Commissioner determined a deficiency on the ground that the claimed liquidating distribution was in substance a taxable sale of her interest to the remaining partners pursuant to Section 741 of the Code. (Pet. App. 27–28.) The district court granted summary judgment for the petitioner, holding as a matter of law that the transactions here involved resulted in a nontaxable distribution in liquidation of petitioner's partnership interest (Pet. App. 26). On appeal, the Fifth Circuit held that the tax consequences of the interrelated series of transactions could not be determined by viewing each transaction in isolation, but instead required consideration of each step as a component part of an overall plan (Pet. App. 31). Applying that standard, the court of appeals noted that the transactions here were so designed that petitioner's undivided 50/225 interest in the Pine Forest Apartments ultimately found its way back into the partnership now owned by the Blairs, and held that, since

[2] The first three transactions all took place on November 30, 1962. The exact date of the fourth transaction is unknown; it was stipulated, however, in the court of appeals that it took place no later than January 31, 1963. (Pet. App. 29.)

this step was an indispensable ingredient in the overall plan, the entire transaction constituted a sale rather than a Section 736 liquidation (Pet. App. 33–35).

ARGUMENT

The decision below is correct. There is no conflict of decisions or any other reason for further review by this Court.

1. In holding that the substance of the planned series of transactions whereby the petitioner withdrew from the Pine Forest partnership was a taxable sale of her partnership interest to the remaining partners, the court of appeals reached the only conclusion compatible with the uncontroverted facts of this case. Section 741 of the Internal Revenue Code of 1954 (Pet. App. 39–40) provides that the gain or loss on a sale or exchange of an interest in a partnership shall be recognized by the transferor partner. On the other hand, Section 736(b) of the Code (Pet. App. 39) provides that payments to a partner by a partnership in liquidation of the partner's interest are considered to be a distribution by the partnership and as such are (with certain exceptions not applicable here) nontaxable under Section 731(a) (Pet. App. 39). "Liquidation of a partner's interest" is defined in Section 761(d) (Pet. App. 40) as the termination of a partner's entire interest by means of a distribution by the partnership to the partner. Thus, the distinction between Section 741 and Section 736 is that the latter provision applies only to payments made by the partnership in exchange for the partnership interest of a retiring partner and does not apply to transac-

tions between the partners. See Treasury Regulations § 1.736–1(a) (Pet. App. 40–41).

The court of appeals correctly concluded that, in substance, the petitioner sold her interest to Mr. and Mrs. Blair. At the end of the series of integrated transactions, the partnership property purportedly distributed to petitioner in liquidation of her interest was back in the partnership and the continuing partners, through their wholly owned corporation, had, in effect, purchased petitioner's interest for $200,000 cash.[3] Simply stated, there were no payments (and hence no liquidating distribution) by the *partnership* and therefore no basis for the application of Section 736(b). The round-robin transfer of the Pine Forest property from the partnership to the petitioner, to the estate of her husband, to the Blair corporation, and back to the partnership was, as the Court of Appeals properly held, merely a facade erected to disguise the true nature of the transaction. See *Commissioner* v. *Court Holding Co.*, 324 U.S. 331; *Minnesota Tea Co.* v. *Helvering*, 302 U.S. 609; *Waterman Steamship Corp.* v. *Commissioner*, 430 F. 2d 1185 (C.A. 5), certiorari denied, 401 U.S. 939; *United States* v. *General Geophysical*, 296 F. 2d 86 (C.A. 5), certiorari denied, 369 U.S. 849.

Petitioner asserts (Pet. 7–8) that the holding of the court below subverts the Congressional policy with respect to the tax treatment of retiring partners. There is no question that, in enacting Sections 736

[3] Under this theory, of course, petitioner would be deemed to have purchased the property from her husband's estate with the $200,000.00 paid to her by Mr. and Mrs. Blair.

and 741 and the other partnership provisions as part of the Internal Revenue Code of 1954, Congress intended to allow partners to decide among themselves whether a partner's withdrawal from a partnership shall be by the "sale" route or the "liquidation" route. Indeed, the court of appeals expressly acknowledged (Pet. App. 35) the right of partners to choose between selling and liquidating. In the instant case, however, petitioner's tax difficulties arose solely from her unwillingness, for economic considerations which she deemed important, to make a straight-forward transfer of her partnership interest in exchange for payments from the partnership in liquidation of that interest; instead, she chose to be paid, in effect, by the individual partners. Accordingly, the court of appeals correctly recognized that the tax consequences of petitioner's withdrawal depended upon the route which the parties actually took, and not upon the label which petitioner seeks to attach to the transactions.

2. The holding of the court below is not in conflict with the decision of the Third Circuit in *Foxman* v. *Commissioner*, 352 F. 2d 466, as petitioner contends (Pet. 6–8). Indeed, *Foxman* is entirely consistent with the decision here. *Foxman* involved payments made to a retiring partner in the form of checks and notes issued by the partnership, undr circumstances where it was to the tax advantage of the continuing partners to have the transaction treated as a liquidation of the interest of the retiring partner, but such liquidation treatment would have resulted in adverse tax consequences to the retiring partner. In that case, the continuing partners argued that since the payments to the retiring

partner were made in the form of checks and notes issued by the partnership, the transaction must be treated for tax purposes as a Section 736 liquidation. The court of appeals rejected this argument as unduly emphasizing form over substance, in contravention of this Court's decision in *Commissioner* v. *Court Holding Co., supra*. The court went on to affirm the Tax Court's decision that, in substance, the payments there in question were made by the remaining partners, and, accordingly the transaction was a sale. Similarly, the Fifth Circuit here has followed the mandate of *Court Holding Co.* in determining that the substance and net effect of the series of integrated transactions was a sale of the petitoner's partnership interest.

3. Petitioner also relies (Pet. 8–13) on cases arising under Section 1031(a) (Pet. App. 40) to establish a basis for review of the decision below. In those cases, the courts have held that certain three-party exchanges of like-kind property involving simultaneous purchases and exchanges qualify for the nonrecognition of gain treatment afforded by Section 1031. The transaction in the present case cannot, however, be characterized as merely a three-cornered exchange of property, as petitioner suggests. Rather, the instant case involves the disposition of the petitioner's partnership interest, the tax consequences of which are controlled by the specific partnership provisions of the Code and not by Section 1031. The issue before the court below was whether the petitioner, in substance, had effected a taxable sale of her interest or a nontaxable liquidation of that interest. That issue cannot be determined by viewing each of the interrelated

transfers in isolation instead of considering them as an integrated whole.[4]

4. Finally, petitioner argues (Pet. 13–18) that the decision below erroneously applied the "substance versus form" doctrine as amplified and explained by this Court in *Commissioner* v. *Court Holding Co., supra,* and *United States* v. *Cumberland Public Service Co.,* 338 U.S. 451. The ultimate question in each of those cases was whether a sale of corporate assets was made by the corporation or by its shareholders in their individual capacity. This Court, in *Court Holding,* affirmed the finding of the Tax Court that the substance of the transaction was a sale by the corporation. In reaching its decision, the Court made its well-known statements that the (p. 334) "incidence of taxation depends upon the substance of a transaction" and that tax liabilities cannot be altered by "mere formalisms." The decision in *Cumberland,* affirming the finding of the Court of Claims that the transaction there was a sale by the shareholders, did not retreat from the legal principles in *Court Holding,* as petitioner suggests. Rather, the court merely pointed out (pp. 454–455) that its language in *Court Holding* did not mean that a corporation could be taxed even where the sale has been made by its stockholders following a *genuine* liquidation and dissolution. The uncontroverted facts here establish that the court of appeals correctly concluded, consistent with

[4] The petitioner's allegation (Pet. 10) that the decision below is in conflict with other decisions of the Fifth Circuit is without foundation. In any event, intra-circuit conflict is not a valid ground for review by this Court. See *Wisniewski* v. *United States,* 353 U.S. 901.

the *Court Holding* and *Cumberland* decisions; that there was no genuine liquidation of petitioner's partnership interest.

CONCLUSION

The petition for certiorari should be denied.

Respectfully submitted.

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